

REPORT OF EXAMINATION
OF

THE WAWANESA MUTUAL
INSURANCE COMPANY
(U.S. BRANCH)

AS OF
DECEMBER 31, 2004

Filed June 1, 2006

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Los Angeles, California
April 14, 2006

Honorable John Garamendi
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of

THE WAWANESA MUTUAL INSURANCE COMPANY (U.S. BRANCH)

(hereinafter also referred to as the Company) at its home office located at 9050 Friars Road, San Diego, California 92108.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2001. This examination covers the period from January 1, 2002 through December 31, 2004. The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions within the examination period, and an evaluation of assets and a determination of liabilities as of December 31, 2004, as deemed necessary under the circumstances.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: corporate records; fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in force by states; loss experience; accounts and records; and sales and advertising.

This examination was conducted concurrently with the examination of the Company's wholly-owned subsidiary, Wawanesa General Insurance Company.

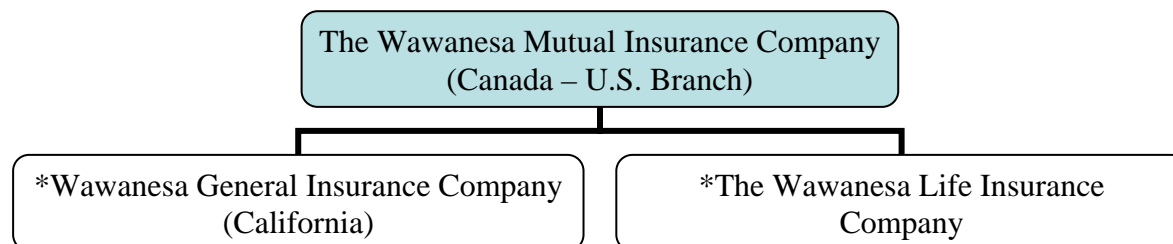
COMPANY HISTORY

The U.S. Branch of the Wawanesa Mutual Insurance Company was established on May 23, 1974, through a \$1 million contribution by the Canadian parent, as a required statutory deposit, with the Insurance Commissioner of the State of California. The first policy was written by the U.S. Branch in April of 1975.

On May 5, 2003, the Company was granted approval to withdraw \$50 million from its U.S. trusteed surplus.

MANAGEMENT AND CONTROL

The following is an abbreviated organization chart of the ultimate parent and its subsidiary insurance companies:



(*) all ownership is 100%

Management of the Company is vested in an eleven-member board of directors elected annually. A listing of the members of the board and principal officers serving on December 31, 2004 follows:

Directors

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
William John Antliff Bulman Winnipeg, Manitoba, Canada	Chairman of the Board The Wawanesa Group of Companies
Richard Ramsay Bracken Winnipeg, Manitoba, Canada	Chairman and Director Royal Canadian Securities
Delmore Clair William Crewson Winnipeg, Manitoba, Canada	Retired
Gregory Joseph Hanson Winnipeg, Manitoba, Canada	Chief Executive Officer and President The Wawanesa Group of Companies
Barry Wayne Harrison Calgary, Alberta, Canada	President and Director Eastgate Minerals Ltd.
Duncan McFarlen Jessiman Winnipeg, Manitoba, Canada	Director Bison Transport
John Stuart McCallum Winnipeg, Manitoba, Canada	Professor The University of Manitoba
Margot Elizabeth Northey Kingston, Ontario, Canada	Retired
Alan Brian Ransom Margeret, Manitoba, Canada	Principle EBM Associates
David Gerhard Unruh West Vancouver, British Columbia, Canada	Retired
Susan Madeline Van De Velde Mariapolis, Manitoba, Canada	Retired

Principal Officers

<u>Name</u>	<u>Title</u>
Gregory Joseph Hanson	President and Chief Executive Officer
George Nicholas Bass	Secretary and General Counsel
Kenneth Ernest McCrea	Vice President and Chief Financial Officer
David Jack Goss	Vice President, U.S. Operations
Brett Alexander MacKinnon	Vice President and Chief Actuary
Paul Robert Goodman	Vice President and Comptroller

Management Agreements

Affiliated Management Agreement: The Company is party to a management agreement dated July 11, 1996 with its subsidiary, Wawanesa General Insurance Company (WGIC). Under this agreement, the Company offers the following services to WGIC: management, office space, information systems, data processing services, telecommunications, administration, financial services, accounting services, investment services, accounting and financial reports, actuarial services, human resources services, legal services, marketing and solicitation of potential insureds, investigation of the applicants, policy forms, underwriting, rating, and claims services. The Company is reimbursed for some expenses on an actual costs basis, while certain expenses are reimbursed on a mutually agreed upon allocation basis. During the examination period a total of \$64.7 million in allocated and direct costs were charged to WGIC by the Company. This agreement was approved by the California Department of Insurance (CDI) on July 25, 1996.

Investment Management Agreement: The Company has an agreement with Deutsche Asset Management (Deutsche) to manage the Company's investments. Under this agreement, Deutsche receives fees based on the market value of the Company's investments.

Trust Agreement: As a condition of writing business in California, the Company is required to maintain in the United States trustee assets for the security of its policyholders and creditors. In order to satisfy this requirement, the Company executed a trust agreement with the Bank of New York. All of the trustee assets are held in the State of California. As of December 31, 2004 the trust had a balance of \$181 million in gross assets and a trustee surplus of \$128 million. This agreement was approved by the CDI on February 7, 2006.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2004, the Company was licensed to transact multiple lines of property and casualty insurance in California. In 2004, direct premiums written were \$69.3 million. The lines of business written were private passenger auto liability (52.3%), auto physical damage (41.8%), homeowners multiple peril (5%) and the remainder, in fire, allied lines, inland marine and earthquake.

REINSURANCE

Assumed

The Company has no reinsurance assumed business.

Ceded

The Company and its subsidiaries are insured under a catastrophe excess of loss reinsurance program. The business covered includes personal, farm, commercial property and commercial automobile physical damage excluding collision; with the following layers of reinsurance:

<u>Layer</u>	<u>Reinsurance Limit</u>
Underlying Catastrophe Cover	95% of \$7.5 million excess of \$17.5 million per occurrence
1 st Catastrophe Cover	95% of \$25 million excess \$25 million
2 nd Catastrophe Cover	95% of \$50 million excess of \$50 million
3 rd Catastrophe Cover	95% of \$50 million excess of \$100 million
4 th Catastrophe Cover	95% of \$50 million excess of \$150 million
5 th Catastrophe Cover	\$200 million excess of \$200 million

All of the treaties are primarily reinsured by Underwriters at Lloyd's of London.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2004

Underwriting and Investment Exhibit for the Year Ended December 31, 2004

Reconciliation of Surplus as Regards Policyholders
from December 31, 2001 through December 31, 2004

Statement of Trusteed Surplus in the United States
for the Year Ended December 31, 2004

Statement of Financial Condition
as of December 31, 2004

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 178,507,190	\$	\$ 178,507,190	
Real estate:				
Properties occupied by the company	14,253,013		14,253,013	
Cash and short-term investments	3,414,444		3,414,444	
Premiums and Considerations:				
Uncollected premiums and agents' balances in course of in the course of collection	976,751		976,751	
Deferred Premiums, agents' balances and installments booked but deferred and not yet due	11,763,717		11,763,717	
Current federal income tax recoverable	22,619		22,619	
Net deferred tax asset	4,351,988	1,399,346	2,952,642	
Electronic data processing equipment and software	393,763		393,763	
Investment income due and accrued	1,897,193		1,897,193	
Other assets non-admitted	810,617	810,617		
Receivables from parent, subsidiaries and affiliates	1,760,036		1,760,036	
Aggregate write-ins for other than invested assets	<u>73,110</u>	<u>62,231</u>	<u>10,879</u>	
Total assets	<u>\$ 218,224,441</u>	<u>\$ 2,272,194</u>	<u>\$ 215,952,247</u>	
<u>Liabilities, Surplus and Other Funds</u>				
Losses			\$ 18,869,024	(1)
Loss adjustment expenses			3,946,083	(1)
Other expenses			1,088,681	
Taxes, licenses and fees			431,151	
Unearned premiums			34,815,111	
Advance premiums			634,445	
Ceded reinsurance premiums payable			217,488	
Amounts withheld or retained by company for account of others			1,546,473	
Drafts outstanding			3,758,874	
Aggregate write-ins for liabilities			<u>656,603</u>	
Total liabilities			65,963,933	
Aggregate write-ins for other than special surplus funds		\$ 1,000,000		
Unassigned funds (surplus)		<u>148,988,314</u>		
Surplus as regards policyholders			<u>149,988,314</u>	
Total liabilities, surplus and other funds			<u>\$ 215,952,247</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2004

Statement of Income

Underwriting Income

Premiums earned		\$ 69,743,924
Deductions:		
Losses incurred	\$ 46,353,031	
Loss expenses incurred	8,828,517	
Other underwriting expenses incurred	<u>6,205,898</u>	
Total underwriting deductions		<u>61,387,446</u>
Net underwriting gain		8,356,478

Investment Income

Net investment income earned	\$ 10,066,928	
Net realized capital gains	<u>1,581,549</u>	
Net investment gain		<u>11,648,477</u>

Other Income

Net gain from agents' or premium balances charged off	\$ 609	
Finance and service charges not included in premiums	<u>789,380</u>	
Total other income		<u>789,989</u>
Net income before federal income taxes		20,794,944
Federal income taxes incurred		<u>6,951,239</u>
Net income		<u>\$ 13,843,705</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2003		\$ 135,474,545
Net income	\$ 13,843,705	
Change in net deferred income tax	1,923,916	
Change in nonadmitted assets	<u>(1,253,852)</u>	
Change in surplus as regards policyholders for the year		<u>14,513,769</u>
Surplus as regards policyholders, December 31, 2004		<u>\$ 149,988,314</u>

Reconciliation of Surplus as Regards Policyholders
from December 31, 2001 through December 31, 2004

Surplus as regards policyholders, December 31, 2001, per Examination	\$162,321,489
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	Gain in Surplus	Loss in Surplus
Net income	\$ 37,858,664	\$
Change in nonadmitted assets		1,286,819
Change in net deferred income tax	1,094,980	
Net remittances to home office	1,094,980	\$ 50,000,000
Totals	\$ 38,953,644	\$ 51,286,819

Net decrease in surplus as regards policyholders	<u>(12,333,175)</u>
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Surplus as regards policyholders, December 31, 2004, per Examination	<u>\$149,988,314</u>
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Statement of Trusteed Surplus in the United States
for the Year Ended December 31, 2004

Assets

General state deposit:	
California Insurance Code Section 1591(a)	\$ 1,883,554
Trusteed assets	<u>177,506,053</u>
 Total gross assets in United States deposited with	
Insurance Department	179,389,607
Interest due and accrued	<u>1,854,388</u>
 Total gross assets within the United States	<u>181,243,995</u>

Liabilities and Reserves

Total liabilities and reserves	65,963,933
 Deductions:	
Agents balances not more than 90 days past due	<u>12,740,468</u>
 Net liabilities	<u>53,223,465</u>
 Trusteed surplus	<u>\$ 128,020,530</u>

The Company maintains trusteed assets in the State of California pursuant to California Insurance Code Section 1591(a).

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

Based on an analysis by a Casualty Actuary from the California Department of Insurance, the Company's loss and loss adjustment expense reserves as of December 31, 2004 were found to be reasonably stated and have been accepted for purposes of this examination.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

None

Previous Report of Examination

None

ACKNOWLEDGEMENT

The courtesy and cooperation extended by the Company's officers and employees during the course of this examination are hereby acknowledged.

Respectfully submitted,

_____/S/_____
Gint Prismantas, CFE
Examiner-In-Charge
Senior Insurance Examiner
Department of Insurance
State of California